

Before the  
Federal Communications Commission  
Washington, D.C. 20554

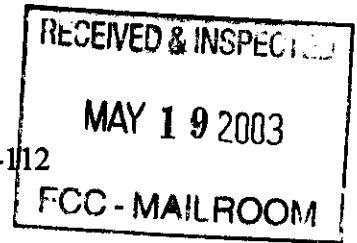
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In the Matter of )

Section 272(f)(1) Sunset of the BOC Separate  
Affiliate and Related Requirements )

WC Docket No. 02-112

2000 Biennial Regulatory Review )  
Separate Affiliate Requirements of Section )  
64.1903 of the Commission's Rules )

CC Docket No. 00-175

### FURTHER NOTICE OF PROPOSED RULEMAKING

Adopted: May 15, 2003

Released: May 19, 2003

**Comment Date: 30 days after Federal Register publication of this Notice****Reply Date: 60 days after Federal Register publication of this Notice**

By the Commission: Commissioners Copps and Adelstein concurring and issuing a joint  
statement.

#### I. INTRODUCTION

1. In this proceeding, we seek comment on the appropriate classification of Bell Operating Companies' (BOCs) and incumbent independent local exchange carriers' (independent LECs) provision of in-region, interstate and international interexchange telecommunications services.<sup>1</sup> We seek comment on how changes to the competitive landscape within the interexchange market should affect this classification and on what approach is appropriate for BOCs and independent LECs, if and when these carriers may provide in-region, interexchange services outside of a separate affiliate.

2. We propose to address the appropriate classification of a BOC's in-region, interstate and international interexchange telecommunications services provided outside of a

<sup>1</sup> In this Further Notice, we seek comment on issues relating to BOCs' and independent LECs' provision of domestic and U.S. international interexchange telecommunications services; however, we do not intend, in this docket, to address the classification of BOCs or independent LECs as "dominant" on specific routes in their provision of international services under 47 C.F.R. § 63.10 of the Commission's rules, which addresses foreign carrier affiliations.

section 272 separate affiliate.<sup>2</sup> Specifically, we seek comment on the continued need for dominant carrier regulation of BOCs' in-region, interstate and international interexchange telecommunications services after sunset of the Commission's section 272 structural and related requirements in a state.<sup>3</sup> In addition, with respect to independent LECs, we note that the Commission initiated a Notice of Proposed Rulemaking in the *2000 Biennial Regulatory Review* proceeding that sought comment on whether to eliminate the separate affiliate requirements imposed on certain independent LECs when they provide in-region, interstate or international interexchange telecommunications services.<sup>4</sup> We ask whether we should classify independent LECs as non-dominant or dominant in their provision of in-region, interstate and international interexchange telecommunications services if the Commission eliminates or modifies the separate affiliate requirements currently imposed on independent LECs.

3. We also ask parties to comment on whether there are alternative regulatory approaches, in lieu of dominant carrier regulation, that the Commission could adopt to detect or deter any potential anticompetitive behavior. We seek comment on the relative benefits and burdens of various approaches. We note that the Commission traditionally has distinguished between BOCs and independent LECs in the past. We recognize that for the issues raised in this rulemaking, different treatment may be warranted for BOCs and independent LECs. We find, however, that there are efficiencies to be gained by considering at the same time the application of these issues to BOCs and independent LECs.

## II. BACKGROUND

4. In a series of orders in the *Competitive Carrier* proceeding, the Commission established a regulatory framework to distinguish between two kinds of carriers – those with market power (dominant carriers) and those without market power (non-dominant carriers).<sup>5</sup> The

<sup>2</sup> 47 U.S.C. §§ 272(a)-(h) (1996). See *Section 272(f)(1) Sunset of the BOC Separate Affiliate and Related Requirements*, WC Docket No. 02-112, Notice of Proposed Rulemaking, 17 FCC Rcd 9916 (2002) (*Section 272 NPRM*); see also *Section 272(f)(1) Sunset of the BOC Separate Affiliate and Related Requirements*, WC Docket No. 02-112, Memorandum Opinion and Order, 17 FCC Rcd 26,869 (2002) (*Section 272 Order*).

<sup>3</sup> The Commission has concluded that section 272(f)(1) provides for a state-by-state sunset of the separate affiliate requirements. 47 U.S.C. § 272(f)(1). See *Section 272 Order*, 17 FCC Rcd at 26,876, para. 13. By operation of law, on December 23, 2002, the section 272 separate affiliate and related requirements sunset for Verizon for the state of New York. See *Public Notice, Section 272 Sunsets for Verizon in New York State by Operation of Law on December 23, 2002 Pursuant to Section 272(f)(1)*, WC Docket No. 02-112, 17 FCC Rcd 26,864 (2002), *petition for review pending sub nom, AT&T Corp., v. FCC*, No. 03-1035 (D.C. Cir. filed Feb. 21, 2003). Verizon has advised the Commission that it is continuing to provide in-region, domestic interstate and international interexchange telecommunications services through a section 272-compliant affiliate. See Letter from Gerald Asch, Director, Federal Regulatory, Verizon to Carol Matthey, Deputy Bureau Chief, Wireline Competition Bureau, Federal Communications Commission, CC Docket No. 96-149 (filed January 13, 2003).

<sup>4</sup> *2000 Biennial Regulatory Review Separate Affiliate Requirements of Section 64.1903 of the Commission's Rules*, CC Docket No. 00-175, Notice of Proposed Rulemaking, 16 FCC Rcd 17,270 (2001) (*2000 Biennial Regulatory Review*).

<sup>5</sup> *Policy and Rules Concerning Rates for Competitive Common Carrier Services and Facilities Authorizations Therefor*, CC Docket No. 79-252, Notice of Inquiry and Proposed Rulemaking, 77 FCC 2d 308 (1979); First Report (continued....)

Commission determined that interexchange carriers affiliated with independent LECs<sup>6</sup> would be regulated as non-dominant provided that the affiliate providing interstate interexchange services: (1) maintain separate books of account; (2) not jointly own transmission or switching facilities with its affiliated exchange telephone company; and (3) acquire any services from its affiliated exchange telephone company at tariffed rates, terms, and conditions.<sup>7</sup>

5. After the passage of the 1996 Act, the Commission, in the *LEC Classification Order*, revisited the appropriate regulatory treatment of BOC affiliates' and independent LECs' provision of interstate and international interexchange services.<sup>8</sup> The Commission determined that dominant carrier regulation should be imposed on a carrier only if it could unilaterally raise and sustain prices above competitive levels and thereby exercise market power by restricting its output<sup>9</sup> or by its control of an essential input.<sup>10</sup> The Commission concluded that, in light of the

(Continued from previous page)

and Order, 85 FCC 2d 1 (1980) (*Competitive Carrier First Report and Order*); Further Notice of Proposed Rulemaking, 84 FCC 2d 445 (1981); Second Further Notice of Proposed Rulemaking, FCC 82-187, 47 Fed. Reg. 17,308 (1982); Second Report and Order, 91 FCC 2d 59 (1982) (*Competitive Carrier Second Report and Order*); Order on Reconsideration, 93 FCC 2d 54 (1983); Third Further Notice of Proposed Rulemaking, 48 Fed. Reg. 28,292 (1983); Third Report and Order, 48 Fed. Reg. 46,791 (1983); Fourth Report and Order, 95 FCC 2d 554 (1983) (*Competitive Carrier Fourth Report and Order*), vacated, *AT&T v. FCC*, 978 F.2d 727 (D.C. Cir. 1992), cert. denied, *MCI Telecommunications Corp. v. AT&T*, 509 U.S. 913, 112 S. Ct. 3020 (1993); *Policy and Rules Concerning Rates for Competitive Carrier Services and Facilities Authorizations Therefor*, CC Docket No. 79-252, 98 FCC 2d 1191 (1984) (*Competitive Carrier Fifth Report and Order*); Sixth Report and Order, 99 FCC 2d 1020 (1985), vacated, *MCI Telecommunications Corp. v. FCC*, 765 F.2d 1186 (D.C. Cir. 1985), affirmed, *MCI v. AT&T*, 512 U.S. 218, 114 S. Ct. 2223 (1994) (*Competitive Carrier Sixth Report and Order*) (collectively *Competitive Carrier proceeding*). See 47 C.F.R. §§ 61.3(q), (y).

<sup>6</sup> The Commission determined that an "affiliate" of an independent LEC is a "carrier that is owned (in whole or in part) or controlled by, or under common ownership (in whole or in part) or control with, an exchange telephone company." *Competitive Carrier Fourth Report and Order*, 95 FCC 2d at 575-79, paras. 31-37; *Competitive Carrier Fifth Report and Order*, 98 FCC 2d at 1198, para. 9.

<sup>7</sup> *Competitive Carrier Fifth Report and Order*, 98 FCC 2d at 1198, para. 9. The Commission concluded that any interstate, interexchange services offered directly by an independent LEC or through an affiliate that did not satisfy the separate affiliate requirements specified in the *Fifth Report and Order*, would be subject to dominant carrier regulation. *Id.* The Commission also proposed to regulate any future provision of interLATA services by the BOCs as dominant, until the Commission determined what degree of separation, if any, would be necessary for the BOCs or their affiliates to qualify for non-dominant regulation. *Id.*, 98 FCC 2d at 1198-99, n.23 (citing *United States v. Western Electric Co.*, 552 F. Supp. 131 (D.D.C. 1982) (subsequent history omitted)).

<sup>8</sup> See *Regulatory Treatment of LEC Provision of Interexchange Services Originating in the LEC's Local Exchange Area and Policy and Rules Concerning the Interstate, Interexchange Marketplace*, CC Docket Nos. 96-149 & 96-61, Second Report and Order in CC Docket No. 96-149 and Third Report and Order in CC Docket No. 96-61, 12 FCC Rcd 15,756 (1997) (*LEC Classification Order*), recon. denied, Second Order on Reconsideration and Memorandum Opinion and Order, 14 FCC Rcd 10,771 (1999) (*Second Reconsideration Order*).

<sup>9</sup> *Id.* at 15,802-03, 15,847, paras. 83, 156-157. The Commission has termed this type of market power "Stiglerian" market power. See *id.* at n.214 (citation omitted).

<sup>10</sup> *Id.* at 15,802-03, 15,847-49, paras. 83, 158-161. A carrier may be able to unilaterally raise prices by increasing its rivals' costs or by restricting its rivals' output through the carrier's control of an essential input, such as access to (continued....)

separation and other requirements of sections 271 and 272 of the Act, and other existing Commission rules,<sup>11</sup> the BOC interLATA affiliates lacked such ability, and therefore should be classified as non-dominant in their provision of in-region, interstate and international interLATA services.<sup>12</sup> The Commission emphasized that its decision to accord non-dominant treatment to the BOC interLATA affiliates' provision of interexchange services was predicated on the presence of a section 272 separate affiliate and full compliance with the structural, transactional, and nondiscrimination requirements of section 272 and the Commission's implementing rules.<sup>13</sup>

6. In the *LEC Classification Order*, the Commission also classified independent LECs as non-dominant in their provision of in-region, interstate and international interexchange services, concluding that these carriers do not have the ability profitably to raise and sustain prices of these services above competitive levels by restricting their own output of these services.<sup>14</sup> In doing so, the Commission determined that some level of separation between an independent LEC's interstate long distance service operations and its local exchange operations was necessary to guard against cost misallocation, unlawful discrimination, or a price squeeze.<sup>15</sup> (Continued from previous page)

bottleneck facilities, which its rivals need to offer their services. The Commission has termed this type of market power "Bainian" market power. See *id.* at n.214 (citation omitted).

<sup>11</sup> The Commission adopted rules to implement the statutory requirements of section 272 in the *Accounting Safeguards Order* and the *Non-Accounting Safeguards Order*. See *Implementation of the Accounting Safeguards Under the Telecommunications Act of 1996*, CC Docket No. 96-150, Report and Order, 11 FCC Rcd 17,539 (1996) (*Accounting Safeguards Order*), Order on Reconsideration, 14 FCC Rcd 11,396 (1996); Second Order on Reconsideration, 15 FCC Rcd 1161 (2000); *Implementation of the Non-Accounting Safeguards of Section 271 and 272 of the Communications Act of 1934, as amended*, CC Docket No. 96-149, First Report and Order and Further Notice of Proposed Rulemaking, 11 FCC Rcd 21,905 (1996) (*Non-Accounting Safeguards Order*); First Order on Reconsideration, 12 FCC Rcd 2297 (1997) (*First Order on Reconsideration*), Second Order on Reconsideration, 12 FCC Rcd 8653 (1997) (*Second Order on Reconsideration*), *aff'd sub nom. Bell Atlantic Telephone Companies v. FCC*, 131 F.3d 1044 (D.C. Cir. 1997), Third Order on Reconsideration, 14 FCC Rcd 16,299 (1999) (*Third Order on Reconsideration*).

<sup>12</sup> *LEC Classification Order*, 12 FCC Rcd at 15,762-63, para. 6. The Commission classified BOC affiliates as non-dominant in their provision of in-region, international services unless they are affiliated with a foreign carrier that has the ability to discriminate in favor of the BOC through control of bottleneck services or facilities in a foreign destination market. *LEC Classification Order*, 12 FCC Rcd at 15,838, para. 139.

<sup>13</sup> *LEC Classification Order*, 12 FCC Rcd at 15,835, para. 134. See *Second Reconsideration Order*, 14 FCC Rcd at 10,798, para. 37.

<sup>14</sup> *LEC Classification Order*, 12 FCC Rcd at 15,763, para. 7, 15,862-63, paras. 188-89. See 47 C.F.R. § 63.10. In the *LEC Classification Order*, the Commission used the term "independent LECs" to refer to both independent LECs and their affiliates. *Id.* at 15,759 n.6. The Commission classified independent LECs as non-dominant in their provision of in-region, international services unless they are affiliated with a foreign carrier that has the ability to discriminate in favor of the independent LEC through control of bottleneck services or facilities in a foreign destination market. *LEC Classification Order*, 12 FCC Rcd at 15,863, para. 189.

<sup>15</sup> *LEC Classification Order*, 12 FCC Rcd at 15,842, para. 145 (citing *Implementation of the Non-Accounting Safeguards of Sections 271 and 272 of the Communications Act of 1934, as amended; and Regulatory Treatment of LEC Provision of Interexchange Services Originating in the LEC's Local Exchange Area*, CC Docket No. 96-149, Notice of Proposed Rulemaking, 11 FCC Rcd 18,877, 18,953, para. 158 (1996) (*Non-Accounting Safeguards NPRM*)).

The Commission, therefore, required independent LECs to provide their in-region, interstate and international interexchange services through separate affiliates that satisfy the separation requirements adopted in the *Competitive Carrier Fifth Report and Order*.<sup>16</sup> In the *Second Reconsideration Order*, however, the Commission relaxed these requirements for those independent LECs that provide in-region, interstate and international interexchange services exclusively through resale, by allowing them to do so through a separate corporate division subject to certain safeguards.<sup>17</sup>

7. As a final matter, the *LEC Classification Order* also eliminated the separate affiliate requirements imposed on BOCs and independent LECs as a condition for non-dominant treatment of their provision of out-of-region, interstate interexchange services.<sup>18</sup>

### III. IDENTIFICATION OF BOC AND INDEPENDENT LEC IN-REGION, INTERSTATE AND INTERNATIONAL INTEREXCHANGE MARKETS

8. The first step in assessing the appropriate regulatory requirements for BOC and independent LEC provision of in-region, interstate and international interexchange telecommunications services is to define and analyze the relevant markets in which these carriers provide these services. We then analyze the market power these carriers may possess in the relevant markets for these services.<sup>19</sup> Consistent with Commission precedent, our regulatory response must be guided by a full understanding of the existing market dynamics for these services.<sup>20</sup> There have been significant changes in the competitive landscape since the

<sup>16</sup> *LEC Classification Order*, 12 FCC Rcd at 15,763, para. 7. The 2000 Biennial Regulatory Review proceeding addresses the question of whether continued application of the separation requirements on independent LECs serves the public interest; whether the benefits of these requirements outweigh the regulatory and economic costs involved; and whether there are possible alternative safeguards to sufficiently address any continued concerns. 2000 Biennial Regulatory Review, 16 FCC Rcd at 17,273, para. 8.

<sup>17</sup> *Second Reconsideration Order*, 14 FCC Rcd at 10,777, para. 9; 47 C.F.R. § 64.1903(b)(1). Independent LEC resellers still must maintain separate books of account, comply with the affiliate transaction rules, and acquire any services from the exchange company pursuant to tariff.

<sup>18</sup> *LEC Classification Order*, 12 FCC Rcd at 15,764, para. 9. Subsequent to the Commission's decision in the *LEC Classification Order*, the Chief, International Bureau, similarly determined that the BOCs and independent LECs should be treated as non-dominant in the provision of out-of-region international services. *NYNEX Long Distance Co., et al. and GTE Telecom Incorporated*, Memorandum Opinion and Order, 12 FCC Rcd 11,654, 11,660-61, paras. 11-13 (1997).

<sup>19</sup> See, e.g., *LEC Classification Order*, 12 FCC Rcd at 15,768, para. 16 ("In order to determine that a particular carrier or group of carriers possesses market power, it is first necessary to define the relevant product and geographic markets."); *Motion of AT&T Corp. to be Reclassified as a Non-Dominant Carrier*, Order, 11 FCC Rcd 3271, 3285, para. 19 (1996) (*AT&T Reclassification Order*) (finding that to reclassify AT&T as non-dominant, one must first "assess whether AT&T has market power" in the relevant markets).

<sup>20</sup> As competition has developed in interexchange markets, the Commission has moved from adopting prescriptive regulations to relying on market forces to promote the public interest. See, e.g., *AT&T Reclassification Order*, 11 FCC Rcd at 3291-309, paras. 33-73 (reclassifying AT&T as a non-dominant carrier because it cannot exercise market power within interstate, domestic, interexchange market); *Competition in the Interstate Interexchange Marketplace*, Report and Order, 6 FCC Rcd 5880, 5893-94, para. 72-74 (1991) (detariffing AT&T business services (continued....))

Commission adopted the *LEC Classification Order*,<sup>21</sup> including: (1) BOC authority to offer in-region, interLATA telecommunications services in 41 states (plus the District of Columbia);<sup>22</sup> (2) an increase in bundled telecommunications services offerings; (3) increased offerings of wide-area pricing plans by mobile telephony carriers; (4) limited, but increasing, substitution of mobile wireless service for traditional wireline service, particularly for interstate calls;<sup>23</sup> and (5) increased use of Internet-based applications (e.g., instant messaging, email). Our approach in this Further Notice is to determine the effects of these changes, if any, on our analysis of the interexchange marketplace.

9. In this Further Notice, we follow Commission precedent for assessing market power by first delineating the relevant service and geographic markets in which market power may be exercised.<sup>24</sup> The Commission generally has followed the approach of the *Merger Guidelines* for defining the relevant service and geographic markets.<sup>25</sup> The *Merger Guidelines* define the relevant service market as the smallest group of competing products for which a hypothetical monopolist provider of the services could profitably impose a "small but significant and non-transitory price increase," holding constant the terms of sale of other services.<sup>26</sup>

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because of the competitiveness in this market); *Policy and Rules Concerning the Interstate, Interexchange Marketplace*, Second Report and Order, 11 FCC Rcd 20,730, 20,733, para. 4 (1996) (detariffing long distance services because market forces will generally ensure that rates remain reasonable).

<sup>21</sup> *LEC Classification Order*, 12 FCC Rcd at 15,810-11, 15,815, 15,821-22, 15,825-27, 15,829, paras. 96, 103, 111, 119, 126 (finding that the BOC interLATA affiliates will be unable to raise price by restricting their output upon entry into interLATA markets or soon thereafter).

<sup>22</sup> The Commission has granted Verizon and BellSouth section 271 authority for their entire in-region territories.

<sup>23</sup> *In the Matter of Federal-State Joint Board on Universal Service*, Report and Order and Second Further Notice of Proposed Rulemaking, 17 FCC 24,952, 25,965 (2002) (*recon. pending*) at para. 21 (*Contribution Methodology Order and FNPRM*); *In the Matter of Implementation of Section 6002(B) of the Omnibus Budget Reconciliation Act of 1993*, Seventh Annual Report and Analysis of Competitive Market Conditions With Respect to Commercial Mobile Services, 17 FCC Rcd 12,985, 13,017 (2002) (*Seventh CMRS Competition Report*); *In the Matter of Implementation of Section 6002(B) of the Omnibus Budget Reconciliation Act of 1993*, Sixth Annual Report and Analysis of Competitive Market Conditions With Respect to Commercial Mobile Services, 16 FCC Rcd 13,350, 13,381-83 (2001) (*Sixth CMRS Competition Report*). We note that AT&T reports its Consumer Services segment experienced a 23 percent reduction in revenues and a "mid-teens" percent reduction in calling volumes for the nine months ending September 30, 2002. The Consumer Services segment provides communications services to residential customers including domestic and international long distance; transaction-based long distance; local and local toll; and dial-up Internet access. AT&T attributes these declines to competition and wireless and Internet substitution. AT&T Securities and Exchange Commission Form 10-Q (filed Nov. 13, 2002) at 51

<sup>24</sup> See, e.g., *LEC Classification Order*, 12 FCC Rcd at 15,773, para. 25; *In the Matter of the Merger of MCI Communications and British Telecommunications*, GN Docket No. 96-245, Memorandum Opinion and Order, 12 FCC Rcd 15,351, 15,367-68, para. 34 (1997) (*MCI/BT Merger Order*); *In re Applications of Mountain Wireless, Inc.*, MB Docket No. 02-138, Hearing Designation Order, 17 FCC Rcd 13,914, 13,920, para. 18 (2002).

<sup>25</sup> 1992 Department of Justice/Federal Trade Commission Horizontal Merger Guidelines, (revised April 8, 1997) (*Horizontal Merger Guidelines*), §§ 1.1, 1.2.

<sup>26</sup> *Horizontal Merger Guidelines*, § 1.11.

Similarly, the *Merger Guidelines* identify the relevant geographic market as a region such that a hypothetical monopolist that was the only present or future producer of the relevant service at locations in that region could profitably impose at least “a small but significant and non-transitory” increase in price, holding constant its terms of sale for all services produced elsewhere.<sup>27</sup> The Commission has concluded that the relevant geographic market for long distance services consists of all point-to-point markets.<sup>28</sup> For purposes of administrative practicality and efficiency, the Commission has found that where consumers face similar competitive choices, it can aggregate such markets for the purposes of its market analysis.<sup>29</sup>

#### **A. Relevant Service Market**

##### **1. In-region, Interstate Interexchange Telecommunications Services**

10. The Commission previously defined the relevant service market for purposes of determining whether non-dominant regulation is appropriate as in-region, interstate interexchange telecommunications.<sup>30</sup> In reviewing certain license transfers, it subsequently adopted narrower relevant service markets in the sense that they are broken down by customer class.<sup>31</sup> In this proceeding, we initially consider two broad customer classes: the mass market and the enterprise market.<sup>32</sup> We recognize that the enterprise market could be divided into a small and medium enterprise, and large enterprise markets. We ask parties to comment on whether these customer classes are warranted for rulemaking purposes in this proceeding and whether

<sup>27</sup> *Horizontal Merger Guidelines*, § 1.21.

<sup>28</sup> The relevant point in a point-to-point market is the location of a particular telephone or other telecommunications device; for example, with regard to residential long distance service, the relevant point is each individual customer's residence. *LEC Classification Order*, 12 FCC Rcd at 15,795, para. 68.

<sup>29</sup> *MCI/BT Merger Order*, 12 FCC Rcd at 15,375, para. 51; *Applications of Teleport Communications Group, Transferor, and AT&T Corp., Transferee, for Consent to Transfer of Control of Corporations Holding Point-to-Point Microwave Licenses and Authorizations to Provide International Facilities-Based and Resold Communications Services*, Memorandum Opinion and Order, 13 FCC Rcd 15,326, 15,248 para. 21 (1998); *Application of NYNEX Corp., Transferor, and Bell Atlantic Corp., Transferee, For Consent to Transfer Control of NYNEX Corp. and its Subsidiaries*, Memorandum Opinion and Order, 12 FCC Rcd 19,985, 20,016-17, para. 54 (1997) (*Bell Atlantic/NYNEX Merger Order*). See also *Application of Echostar Communications Corp., General Motors Corp., and Hughes Electronics Corp. Transferors, and Echostar Communications Corp., Transferee*, Hearing Designation Order, 17 FCC Rcd 20,559, 20,610, para. 119 (2002).

<sup>30</sup> See *LEC Classification Order*, 12 FCC Rcd at 15,782-87, paras. 40-51.

<sup>31</sup> See *Application of WorldCom, Inc. and MCI Communications Corp. for Transfer of Control of MCI Communications Corp. to WorldCom, Inc.*, 13 FCC Rcd 18,025, 18,040-42, paras. 24-29 (1998) (*WorldCom/MCI Merger Order*) (defining two customer groups, residential and small business customers (the mass market) and medium and large business customers (larger business market)).

<sup>32</sup> The mass market includes very small businesses. These categorizations are consistent with the Commission's approach in merger orders. See, e.g., *WorldCom/MCI Merger Order*, 13 FCC Rcd at 18,040-41, paras. 26-27; *Application of GTE Corp., Transferor, and Bell Atlantic Corp., Transferee, For Consent to Transfer Control*, CC Docket No. 98-184, Memorandum Opinion and Order, 15 FCC Rcd at 14,032, 14,088-89, para. 102.

these customer classes are appropriate for the in-region, interstate interexchange telecommunications services markets. To the extent commenters propose an alternative market definition, we ask parties to identify not only which services to include within the relevant service market, but whether there should be separate service markets for different customer classes. We also seek comment on whether we need to separately analyze the wholesale and retail markets as separate relevant service markets. Commenters should provide any relevant studies and data that demonstrate the existence of separate mass market and enterprise markets, or that support their proposed relevant service markets.<sup>33</sup>

11. In discussing the relevant service markets which include BOC and independent LEC-provided in-region, interstate interexchange telecommunications services, we ask commenters to consider not only services provided over traditional wireline local telephone networks, but also comparable services provided over other platforms. We note that the term "interstate, interexchange services" includes telecommunications services offered by cable and wireless providers, often as part of bundled offerings.<sup>34</sup> We seek comment on whether these services should be included in the relevant service market for this proceeding, as well as the significance of these providers for any specific customer class.<sup>35</sup> The Commission has taken note in other contexts of the increased offerings of wide-area pricing plans by mobile telephony carriers, and the increased substitution of mobile wireless service for traditional wireline service, especially for interstate interexchange calls.<sup>36</sup> We seek comment on the availability and consumer purchase patterns of these plans, and how the attributes of these plans (e.g., minutes of use limits, time of call, and coverage) as well as any characteristics of traditional wireline and mobile wireless service may affect the substitutability of mobile wireless and traditional wireline calling plans for in-region, interstate interexchange telecommunications services for all customer classes.<sup>37</sup> For example, do capacity limits, reliability concerns and the cost of service limit the

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<sup>33</sup> See *Non-Accounting Safeguards NPRM*, 11 FCC Rcd at 18,934-35, para. 119; *LEC Classification Order*, 12 FCC Rcd at 15,784, para. 44 (noting that "credible evidence" should include information sufficient to identify services that are likely substitutes and the carrier or group of carriers that allegedly possesses market power). Such data may include econometric estimates of cross elasticity of demand or marketing studies that show consumer substitutability of demand for competing services.

<sup>34</sup> All references to mobile telephony refer to all operators that offer commercially available, interconnected mobile phone services. These operators provide access to the public switched telephone network via mobile communication devices principally using spectrum allocations for cellular, broadband PCS, and SMR. See *Seventh CMRS Competition Report*, 17 FCC Rcd at 12,993.

<sup>35</sup> We note that these alternative platforms may be of limited competitive significance. For example, as of June 2002, there were a reported 2.6 million coaxial cable connections being used to provide local exchange service, representing about 1 percent of the nation's switched access lines. In addition, some analysts estimate that 3 to 5 percent of wireless customers use their wireless phone as their only phone. Industry Analysis and Technology Division, Wireline Competition Bureau, Federal Communications Commission, Local Telephone Competition: Status as of June 20, 2002, Table 11 (released Dec. 2002); *Seventh CMRS Competition Report* at 33.

<sup>36</sup> See *infra* note 23.

<sup>37</sup> We note that consumers of mobile wireless services can opt for calling plans in which the marginal price of an in-region, interstate, interexchange call is approximately zero, depending upon the time of the call and whether the customer has expended all of the minutes in the bucket of minutes provided by the calling plan. Moreover, the (continued....)



degree of substitution for in-region, interstate interexchange telecommunications services between mobile wireless and traditional wireline services for enterprise customers? We ask commenters to address the degree of substitutability between in-region, interstate interexchange telecommunications services offered by independent interexchange carriers and incumbent LEC affiliates on the one hand, and the same services offered by these other types of carriers. We also seek comment on whether Internet-based applications should be included in the relevant service markets.<sup>38</sup> Commenters are invited to submit any empirical studies that have analyzed the substitution across these platforms or have estimated the cross-elasticity of demand across these platforms for in-region, interstate interexchange telecommunications services. We also invite comment on any differences in the availability of alternative platforms between BOC and independent LEC regions.

12. We seek comment on the availability of unlimited interstate interexchange calling plans offered by wireline providers, and the impact these bundled offerings have on the relevant service market and any specific customer class.<sup>39</sup> We seek comment on whether bundled offerings that include local and interstate interexchange services constitute a separate relevant service market. We invite comment on whether there are differences in the availability of bundled service packages across BOC and independent LEC regions and how this would affect our analysis.

13. We request comment on whether there is any relevant distinction between a BOC's in-region, interstate, interLATA services and its in-region, interstate, intraLATA services offered post-sunset.<sup>40</sup> We note that the *LEC Classification Order* classified BOC interLATA affiliates as non-dominant in the provision of "in-region, interstate, domestic, interLATA services." We question whether this is the appropriate service market for analyzing BOC in-region, interstate services if both interLATA services and intraLATA services may be provided by a BOC on an integrated basis (*i.e.*, without a separate interLATA affiliate). Would a BOC operating on an integrated basis distinguish between interLATA and intraLATA services? In addition, we seek comment on whether customers distinguish between BOC in-region, interstate

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Commission increased the interim mobile wireless safe harbor for universal service contributions from 15 percent to 28.5 percent to better reflect the extent that mobile wireless is used for interstate calls. *Contribution Methodology Order and FNPRM*, 17 FCC 24,965-66 at paras. 21-22.

<sup>38</sup> See *infra* note 23.

<sup>39</sup> For example, service packages such as MCI's Neighborhood package include unlimited local, toll and long distance calls and several vertical features for a fixed monthly fee.  
[http://www.TheNeighborhood.com/res\\_local\\_service/jsps/default.jsp](http://www.TheNeighborhood.com/res_local_service/jsps/default.jsp) (visited Feb. 19, 2003)

<sup>40</sup> See *Access Charge Reform*, CC Docket Nos. 96-262 et al, Fifth Report and Order and Further Notice of Proposed Rulemaking 14 FCC Rcd 14,221, 14,245, para. 48 (1999)(*Pricing Flexibility Order*) (describing the BOCs' interstate, intraLATA toll services, for which the Commission removed price cap regulation and relaxed tariff requirements but did not make a finding of non-dominance).

services that cross a LATA boundary and those that do not? We request comment on the pros and cons, post-sunset, of shifting our analysis to BOC provision of in-region, interstate services.<sup>41</sup>

14. We seek comment on the impact of competition in upstream local exchange access services markets. Specifically, we ask whether we should analyze separately the relevant service market for downstream services, *i.e.*, the end-user retail long distance services market, and upstream services, *i.e.*, the access services market. In particular, we seek comment on how to evaluate competitive entry into local markets by firms relying on various methods of entry, including self deployment of facilities (*e.g.*, cable telephony), access to network elements and use of spectrum, whether for fixed or mobile services. To what extent has facilities deployment by competitive LECs, fixed and mobile radio service providers, and cable telephony providers reduced incumbent LEC market power over access? We encourage commenters to consider how, if at all, this competitive entry has impacted the upstream access services markets. What impact, if any, does a competitive downstream market have on the upstream access services market? Do the BOCs and incumbent LECs possess market power in access services markets? In addition, we seek comment on whether and how the extent of competition in the access services markets differs across different classes of customers. Would it be useful to distinguish further between BOC and independent LEC in-region and out-of-region access services markets? Finally, has there been any significant change in the market structure of the access services markets since the *LEC Classification Order*?

## 2. In-region, International Interexchange Telecommunications Services

15. In the *LEC Classification Order*, the Commission defined the relevant service market, in the international context, as any international long-distance service for which there are no close substitutes or as any group of services that are close substitutes for each other, but for which there are no other close substitutes.<sup>42</sup> It refrained, however, from delineating specific service markets, noting that it would do so only in cases where there was credible evidence suggesting that there was or could be a lack of competitive performance with respect to a particular service or group of services.<sup>43</sup> Instead, the Commission evaluated market power based on aggregate data for all international services combined. This flexible approach recognizes the dynamic and complex nature of the international telecommunications marketplace, in which offerings available to end users are changing over time.<sup>44</sup> In recent years, however, the Commission has typically identified the following categories as separate end-user markets: (1) mass market customers (including residential and small business customers) and (2) medium and

<sup>41</sup> See also 47 C.F.R. § 63.03(b)(2) (finding relevant, for purposes of streamlining domestic applications for transfer of control, market shares in the "interstate, interexchange" market).

<sup>42</sup> *LEC Classification Order*, 12 FCC Rcd at 15,787-88, para. 54.

<sup>43</sup> *Id.*

<sup>44</sup> See *MCI/BT Merger Order*, 12 FCC Rcd at 15,374-75, para. 49; see also *WorldCom/MCI Merger Order*, 13 FCC Rcd at 18,903-94, para. 119.

large-sized business customers.<sup>45</sup> In certain instances, the Commission has also identified global seamless services<sup>46</sup> as an end-user market.<sup>47</sup> We invite comment on whether these market categories remain appropriate and, if not, in what way they should be revised.

16. Many of the questions asked in this notice regarding the proper delineation of service markets for interstate interexchange telecommunications services apply equally to international services. We request that commenters state whether their answers regarding interstate long-distance service are applicable to international services as well, and, if not, to describe how they differ. Specifically, we ask whether we should analyze separately the relevant service market for downstream services, *i.e.*, the end-user retail international services market, and upstream services, *i.e.*, the access services market. We also ask parties to comment on whether there are unique aspects of international service that would affect the delineation of service markets. For example, Internet-based services may be emerging as an important substitute for traditional calling over many international routes. We ask parties to comment on the degree to which Internet-based services substitute for traditional provision of international services by wireline operators.

## **B. Relevant Geographic Market**

### **1. In-region, Interstate Interexchange Telecommunications Services**

17. We seek comment on the appropriate relevant geographic market for each of the relevant service markets for in-region, interstate interexchange telecommunications services. We note that the Commission has previously identified the relevant geographic market for in-region, interstate interexchange telecommunications services as all possible routes that allow for a connection from one particular location to another particular location ("point to point").<sup>48</sup> The Commission also determined that when a group of point-to-point markets exhibits sufficiently

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<sup>45</sup> See, e.g., *WorldCom/MCI Merger Order*, 13 FCC Rcd at 18,095, para. 122. As a final service consumed by businesses and residential customers, international long-distance service constitutes an "end-user" market that can be distinguished from "input markets," on which they rely, such as local access services and international transport services.

<sup>46</sup> Global seamless services are defined as a combination of voice, data, video, and other telecommunications services that are offered by a single or multiple source over an integrated international network of owned or leased facilities (with either regional or global coverage), and that have the equivalent quality, characteristics, features and capabilities wherever they are provided. See *AT&T Corp., British Telecommunications, plc, VLT Co. L.L.C., Violet License Co. L.L.C., and TNV [Bahamas] Limited, Applications for Grant of Section 214 Authority, Modification of Authorizations and Assignment of Licenses in Connection With the Proposed Joint Venture Between AT&T Corp. and British Telecommunications, plc*, Memorandum Opinion and Order, 14 FCC Rcd 19,140, 19,150-53 (1999), paras. 21-28 (*AT&T/BT Joint Venture Order*).

<sup>47</sup> See *AT&T/BT Joint Venture Order*, 14 FCC Rcd at 19,150-72, paras. 21-61.

<sup>48</sup> *LEC Classification Order*, 12 FCC Rcd at 15,761-61, para. 5.

similar characteristics, we can aggregate the separate point-to-point markets rather than examine each individual point-to-point market separately.<sup>49</sup>

18. Moreover, the Commission has previously determined that unless there is credible evidence indicating that there is or could be a lack of competition in a particular point-to-point market, and there is a showing that geographic rate averaging will not sufficiently mitigate the exercise of market power, the Commission would treat interstate long distance calling as a single national market.<sup>50</sup> The Commission found that price regulation of exchange access services, and the excess capacity in interstate transport would also cause carriers to behave similarly in each interstate point-to-point market.<sup>51</sup> However, the Commission also found that its analysis of the BOCs' and independent LECs' market power should reflect the expectation that the competitive conditions these carriers face will differ between those point-to-point markets that originate in-region and those point-to-point markets that originate out-of-region.<sup>52</sup> We seek comment on whether our analysis should adopt this bifurcated approach. In addition, given the changes in the competitive landscape and current market conditions, is it more appropriate now to aggregate such point-to-point markets on a region-wide, statewide or some other basis?

19. We also invite comment on whether the inclusion of in-region, interstate interexchange calls placed on other platforms would affect the relevant geographic market. Within a geographic area, the size of the local calling area may differ significantly across platforms, or competitors' available facilities may be significantly different. For example, depending upon the wireless calling plan, the local calling area for a mobile wireless customer may be substantially larger than for either traditional wireline service or cable telephony. We invite comment on whether these types of differences would affect our analysis of the relevant geographic market for in-region, interstate interexchange telecommunications services or for any particular customer class.

## **2. In-region International Interexchange Telecommunications Services**

20. In assessing the market power of BOCs and independent LECs in international

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<sup>49</sup> *Id.* at 15,761-62, 15,792-95, 15,799-800, paras. 5, 64-69, 76-78.

<sup>50</sup> *Id.* at 15,794, para. 66. Geographic rate averaging requires a provider of interstate interexchange telecommunications services to provide such services to its subscribers in each state at rates no higher than the rates charged to its subscribers in any other state. 47 U.S.C. § 254(g). Geographic rate averaging and advertising the same prices across geographic markets, may mitigate the ability of a carrier to exercise market power in a particular geographic market if the carrier operates in numerous geographic markets. *Id.* at 15,788, para. 56, *Policy and Rules Concerning the Interstate, Interexchange Marketplace*, CC Docket No. 96-61, Notice of Proposed Rulemaking, 11 FCC Rcd. 7141, 7170, para. 53 (1996).

<sup>51</sup> *Id.* at 15,794-95, paras. 66-67.

<sup>52</sup> *Id.* at 15,799-80, paras. 76-78. Specifically, the Commission expressed the concern that if a BOC interLATA affiliate's or independent LEC's long distance customers are concentrated in one region, it may be profitable for the firm to raise prices above competitive levels, even if geographic rate averaging might cause it to lose market share outside that region. *Id.* At 15,780, para. 77.

service markets, the Commission determined in the *LEC Classification Order* that it was appropriate to examine international point-to-point markets that originate within a BOC's or independent LEC's region separately from point-to-point markets that originate out-of-region, because the BOC's and independent LEC's control of local bottleneck facilities made calls originating in-region competitively distinct from calls originating out-of-region.<sup>53</sup> The Commission further concluded that, within each BOC's or independent LEC's region, it was appropriate to examine aggregate data encompassing all international routes, because the competitive characteristics of in-region international interexchange service provided by a BOC or independent LEC were not likely to differ by route.<sup>54</sup>

21. Many of the questions asked in this notice regarding the proper delineation of geographic markets for interstate interexchange telecommunications services apply equally to international services. We request that commenters state whether their answers regarding interstate long-distance service are applicable to international services as well, and, if not, to describe how they differ. We also ask parties to comment on whether there are unique aspects of international service that would affect the delineation of geographic markets. In particular, we seek comment on whether the framework that the Commission adopted in the *LEC Classification Order* for defining geographic markets remains appropriate.

#### IV. MARKET POWER ANALYSIS

22. We propose to follow the same analytical framework the Commission used in the *LEC Classification Order* to assess the extent of market power that could be exercised by a BOC or independent LEC affiliate providing in-region, interstate and international interexchange telecommunications services as an integrated corporate entity.<sup>55</sup> There, the Commission's focus was on the ability of these carriers' affiliates to unilaterally raise and sustain prices of in-region, interstate and international interexchange telecommunications services above competitive levels in a particular relevant geographic market.<sup>56</sup> We direct commenters to address separately the

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<sup>53</sup> *Id.* at 15,800-01, para. 80.

<sup>54</sup> *Id.* We clarify that, in general, each international route constitutes a distinct geographic market, because the competitive characteristics of point-to-point markets on any given route are usually identical and the competitive characteristics of an individual route typically differ from those of other routes. *See International Competitive Carrier Policies*, 102 FCC 2d 812 (1985), *recon. denied*, 60 RR 2d 1435 (1986); *see also LEC Classification Order*, 12 FCC Rcd at 15,800-01, para. 80. ("We acknowledge that myriad factors...may affect our determination of whether each international point-to-point market has competitive characteristics that are sufficiently similar to other point-to-point markets in the international marketplace.") For the purpose of analyzing market power of a particular carrier, however, it may be reasonable to evaluate aggregated data from all international routes if there is convincing evidence that the carrier's market power does not vary across routes. *See Motion of AT&T Corp. to be Declared Non-Dominant for International Service*, Order, 11 FCC Rcd 17,963, 17,974-75, (1996) paras. 31-32.

<sup>55</sup> In the *LEC Classification Order*, the Commission considered the likelihood of anticompetitive behavior arising from traditional market power factors and control of bottleneck access facilities for both the BOCs and independent LECs. *LEC Classification Order*, 12 FCC Rcd at 15,809-33, 15,847-15,857, paras. 93-130, 156-175.

<sup>56</sup> *Id.* at 15,802-04, 15,847-15,857, paras. 83-85, 156-175.

potential effects in the interstate markets and international markets. Specifically, we seek comment on any differences in parties' assessment of these carriers' incentives and abilities to exercise market power in any of the aforementioned interstate interexchange relevant markets as opposed to any of the aforementioned international interexchange relevant markets when these services are provided on an integrated basis.

23. As discussed above, the long distance marketplace is in a period of significant transition. Comments should reflect current conditions and those that are likely to exist in the near term.<sup>57</sup> Chiefly, as BOCs obtain section 271 authority in all of their in-region states, they are able to become significant players in the long distance (including international) markets.<sup>58</sup> Receiving section 271 authority for their entire region also permits BOCs to provide long distance service to large enterprise customers, something they could not previously do as a practical matter because of their inability to provide long distance service nationwide. The Commission based its non-dominance finding for the BOC section 272 affiliates in part on the affiliates' lack of in-region, interstate interexchange telecommunications services market share upon their entry or soon after their entry into this market.<sup>59</sup> We seek comment on how the BOCs' increasing presence in the long distance market for any customer class should affect our analysis.

24. We also invite comment on how market concentration and pricing have changed over time in any relevant service or geographic market and how this should affect our analysis of market power. The most recent long distance data reported by the Commission suggests that the BOCs' entry into in-region long distance may significantly affect the market structure of the long distance industry over time. These data suggest that the nationwide residential market share for AT&T has fallen, while the market share for MCI and Sprint has increased over time.<sup>60</sup> These data also suggest that the BOCs have been able to gain significant market share after they receive section 271 authority.<sup>61</sup> We invite comments on these market developments, and on how we

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<sup>57</sup> See paragraph 8.

<sup>58</sup> For the consumer market, TNS estimates that Verizon is now the third largest long distance provider in terms of households and fourth largest in terms of revenues. Press Release, *TNS Telecoms Data Ranks Verizon Third Largest Long Distance Provider In U.S., Surpassing Sprint*, Jan. 7, 2003.

<sup>59</sup> *LEC Classification Order*, 12 FCC Rcd at 15,810-11, 15,815, 15,821-22, 15,825-27, 15,829, paras. 96, 103, 111, 119 and 126 (finding that BOC interLATA affiliates would not have the ability to raise price by restricting their output upon entry or soon thereafter).

<sup>60</sup> Industry Analysis and Technology Division, Wireline Competition Bureau, *Statistics of the Long Distance Telecommunications Industry* (May 2003), Table 14 (released May 14, 2003). For example, measured in access lines, AT&T's residential market share has declined from 74.6 percent in 1995 to 36.7 percent in 2002. Over this time period, the market share for MCI has increased from 13 percent to 15.8 percent, and the market share for Sprint has increased from 4.2 percent to 7.6 percent.

<sup>61</sup> *Id.* at Table 15. According to the Commission report, as of 2002, Verizon had a 9.3 percent share of residential households, SBC had a 3.8 percent share of residential households, and BellSouth had a 0.2 percent share of residential households. The data suggest that the BOCs' market shares vary significantly across regions. Notably, the data suggest that Verizon had a 28.4 percent share in the Northeast and SBC had a 23.9 percent share in the Southwest. We note that Verizon and SBC have had section 271 authority for the longest period of time, with (continued....)

should incorporate this information into our assessment of the potential market power of the various competitors in the interstate interexchange market. In addition, we seek comment on whether, if at all, these developments should affect our analysis of the relevant geographic markets.

25. At the same time, there has been an increase in offerings of bundled telecommunications services by major interexchange carriers, cable telephony providers, and the BOCs upon section 271 approval. The Consumer Price Index for long distance charges has declined over the past twelve months,<sup>62</sup> and some have suggested that offerings of bundled telecommunications services have reduced long distance service prices.<sup>63</sup> Press reports, however, indicate that prices for long distance services have increased for some consumer plans in the last year.<sup>64</sup> We invite comments on these trends, and on how we should incorporate this information into our assessment of the potential market power of the various competitors in the interstate interexchange market. In particular, are bundled service package offerings viewed as sufficiently substitutable by a sufficiently large percentage of customers to constrain the exercise of market power by the BOCs and independent LECs? Also, does ownership of facilities, compared to leasing unbundled network elements, affect the ability of bundled service providers to constrain the exercise of market power by BOCs and independent LECs?

26. Within each customer class and relevant service and geographic market, we seek comment on whether the BOCs and independent LECs possess market power and are likely to be able to exercise such power. As noted above, the Commission has previously found that a carrier can unilaterally raise and sustain prices above competitive levels and thereby exercise market power in two ways.<sup>65</sup> First, a carrier may be able to raise prices by restricting its own output if it has a large market share.<sup>66</sup> Second, a carrier may be able to unilaterally raise prices by increasing its rivals' costs or by restricting its rivals' output through the carrier's control of an essential input, such as access to bottleneck facilities, which its rivals need to offer their services.<sup>67</sup>

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Verizon obtaining section 271 approval in New York in 1999, and SBC obtaining section 271 approval for Texas in 2000. *Id.*

<sup>62</sup> See U.S. Department of Labor, Bureau of Labor Statistics, Consumer Price Index for Long Distance Charges, U.S. City Average (extracted Mar. 12, 2003).

<sup>63</sup> See, e.g., Jane Spencer, WALL STREET JOURNAL, *Looming FCC Decision Adds Reason to Rethink Your Plan: Overcoming the Inertia Factor*, Jan. 8, 2003.

<sup>64</sup> See, e.g., Jane Spencer, WALL STREET JOURNAL, *MCI Sets Third Price Rise This Year*, Nov. 22, 2002; Shawn Young, WALL STREET JOURNAL, *AT&T Will Raise Calling Rates, Fees On Long Distance*, Dec. 30, 2002; ; Shawn Young, WALL STREET JOURNAL, *AT&T, WorldCom's MCI Prepare to Levy New Set of Rate Increases*, Jan 3, 2003.

<sup>65</sup> As in previous orders, we refer in the following discussion to a carrier's ability to engage in such a strategy generally as the ability to "raise prices." See, e.g., *LEC Classification Order*, 12 FCC Rcd at 15,803, n.213.

<sup>66</sup> See note 9 *supra*.

<sup>67</sup> See note 10 *supra*.

27. In assessing the first type of market power, the Commission traditionally has focused on certain well-established market features, including market share, supply and demand substitutability, the cost structure, size, and resources of the firm. In the *LEC Classification Order*, the Commission found that an analysis of traditional market factors suggests that the BOC affiliates and the independent LECs did not have the ability profitably to raise and sustain prices above competitive levels by restricting their output.<sup>68</sup> The Commission based this finding on the initially small market share of these carriers compared to the major interexchange carriers; the high supply and demand elasticities for this service; and the low entry barriers in the interexchange market. We invite comment as to whether the Commission should revisit this prior finding in light of current conditions.<sup>69</sup>

28. We seek comment specifically on what factors the Commission should consider in evaluating the market power of the BOCs and independent LECs in the provision of interexchange telecommunications service. We invite comments on what is the best data to use to estimate market share, e.g., revenues, minutes of use, end users, subscribers, etc. We invite commenters to submit any empirical studies that look at the extent of market concentration or estimate the market share for the various interexchange carriers providing services in any of the aforementioned relevant markets. We also invite comment on the extent to which competitors share common ownership with BOCs and independent LECs, and how we should incorporate this information into our analysis of market share in any of the aforementioned relevant markets. For example, how should we factor the BOCs' and independent LECs' interests in their respective mobile telephony operations into our analysis?<sup>70</sup>

29. With respect to the second type of market power, the Commission has focused on a BOC's and independent LEC's ability to exercise market power through its control of local bottleneck facilities.<sup>71</sup> Accordingly, we seek comment on the extent to which these carriers could leverage market power from their local exchange and exchange access markets into the markets for interstate and international interexchange telecommunications services. The Commission previously has found that these carriers might leverage their market power in the local exchange and exchange access markets through cost-misallocation, raising their rivals' costs, improper discrimination to gain an advantage in the interexchange telecommunications services market, or a predatory price squeeze.<sup>72</sup> We seek comment on the incentives and abilities of these carriers to

<sup>68</sup> *Id.* at 15,810-11, 15,847, paras. 96-97, 156-157.

<sup>69</sup> Commenters should consider prior Commission orders in their analysis. See, e.g., *LEC Classification Order*, 12 FCC Rcd at 15,810-33, paras. 96-130; *AT&T Reclassification Order*, 11 FCC Rcd at 3271, 3346-47, para. 139 (concluding that AT&T lacked market power after examining factors such as supply elasticity, demand elasticity, market share, trends in market share and other indicia of market conduct and performance, including price levels and trends in prices over time); *Competitive Carrier First Report and Order*, 85 FCC 2d at 21, para. 57.

<sup>70</sup> See, e.g., Steven Salop and Daniel O'Brien, *Competitive Effects of Partial Ownership: Financial Interest and Corporate Control*, 67 ANTITRUST L.J. 559 (2000).

<sup>71</sup> *LEC Classification Order*, 12 FCC Rcd at 15,812-3, 15,847-49, paras. 98-100, 158-161.

<sup>72</sup> See, e.g., *Applications of Ameritech Corp., Transferor, and SBC Communications Inc., Transferee, for Consent to Transfer Control of Corporations Holding Commission Licenses and Lines Pursuant to Sections 214 and 310(d)* (continued....)



misallocate their costs, discriminate, and engage in predatory price squeezes to such an extent that they may increase their market share and attain market power in the interstate and international interexchange markets. In particular, the Commission raised concerns in the *LEC Classification Order* about the incentive and ability of these carriers to engage in a predatory price squeeze (e.g., by raising the price of their access services but not interstate interexchange prices or by lowering interstate interexchange prices at or below the price of their access services).<sup>73</sup> We ask whether the carriers' incentives and abilities increase if they provide interstate and international interexchange services on an integrated basis.

30. We also seek comment on the abilities and incentives of these carriers to use their market power in the local exchange and exchange access markets to disadvantage rival suppliers of interstate and international services in any way. To the extent that competitors purchase unbundled network elements from these carriers, we also seek comment on the checks that are in place that would hamper or diminish their ability to disadvantage rival suppliers of interstate and international services. We invite comment on the likelihood of these strategic behaviors and whether these strategies would succeed in any of the aforementioned relevant service markets or customer classes.<sup>74</sup>

31. The Commission has previously found that BOCs with section 271 approval will have the ability and the incentive to discriminate against termination of interexchange calls by other carriers.<sup>75</sup> We seek comment on how this incentive will be affected if the service is offered by the integrated BOC entity or by an integrated independent LEC. We also seek comment on whether allowing BOCs and independent LECs to provide interexchange service on an integrated basis will diminish the ability of regulators and interexchange competitors to detect such discrimination.

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of the Communications Act and Parts 5, 22, 24, 63, 90, 95 and 101 of the Commission's Rules, CC Docket No. 98-141, Memorandum Opinion and Order, 14 FCC 14,712, 14,764, 14,795-99, 14,807-17, paras. 107, 186-196, 212-235 (describing the incentives, ability and means for the merged entity to delay interconnection negotiation and dispute resolution, to limit the methods and points of interconnection; and to engage in price and non-price discrimination, such as delaying the provisioning of and degrading the quality of, interconnection) (1999) (*SBC/Ameritech Merger Order*); *LEC Classification Order*, 12 FCC Rcd at 15,815-19, 15,821-26, 15,829-33, 15,847-15,857, paras. 103-108, 111-119, 125-130, 158-175 (describing the incentives, ability and means for an incumbent LEC to improperly allocate costs, engage in price and non-price discrimination, and engage in a price squeeze); *Non-Accounting Safeguards NPRM*, 11 FCC Rcd at 18,886, para. 14 (describing the ability of an incumbent LEC to create a price squeeze and thereby reduce the attractiveness of its competitors' services). See also *Reform of Access Charges Imposed by Competitive Local Exchange Carriers*, Seventh Report and Order and Further Notice of Proposed Rulemaking, CC Docket No. 96-262, 16 FCC Rcd 9923, 9937, para. 34 (2001) (*CLEC Access Charge Order*) (describing market power that competitive LECs have for the rates they tariff for switched access).

<sup>73</sup> *LEC Classification Order*, 12 FCC Rcd at 15,830-33, 15,836-40, 15,847-57, paras. 127-130, 135-142, 156-175.

<sup>74</sup> The success of this strategy may depend upon the relevant service market. For instance, this strategy may only succeed if it results in the exit of providers, and consumers are unable to avoid a subsequent price increase for interstate, interexchange services by increasing the number of these calls placed on a wireless phone.

<sup>75</sup> *SBC/Ameritech Merger Order*, 14 FCC Rcd at 14,799, 14,807-12, paras. 195-96, 212-224.

32. We note that the Commission has granted Phase I and Phase II pricing flexibility in numerous metropolitan statistical areas (MSA) for price cap incumbent LECs.<sup>76</sup> In doing so, the Commission made no finding of non-dominance for carriers that meet these Phase I and Phase II triggers. We seek comment on whether BOCs and independent LECs possess market power with respect to inputs which they could use to raise rivals' costs because these inputs are critical to a firm's ability to provide in-region, interstate and international, interexchange telecommunications services to end user customers.<sup>77</sup> Would the reliance on these carriers by mobile telephony providers, interstate interexchange providers or other competitors for special access and/or transport undermine these competitors' ability to discipline potential BOC or independent LEC anticompetitive behavior?<sup>78</sup>

33. We also consider whether coordinated anticompetitive behavior is possible.<sup>79</sup> The Commission has recognized that coordinated behavior in markets with vigorous competition is difficult.<sup>80</sup> We ask whether the potential for coordinated behavior is affected by a BOC or independent LEC offering in-region, interstate and international interexchange telecommunications services on an integrated basis. We invite comment on how the distribution of market share within any of the aforementioned relevant markets would affect our assessment of the likelihood of coordinated anticompetitive behavior.<sup>81</sup> We also invite comment on the incentives and abilities of competitors to offset a coordinated attempt to sustain an

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<sup>76</sup> The Commission established a framework for granting price cap LECs greater flexibility in the pricing of interstate access services once they satisfy certain triggers to demonstrate that market conditions in a particular area warrant relief. For example, to receive Phase I pricing flexibility for dedicated transport and special access services (other than channel terminations to end users), a price cap LEC must show that unaffiliated competitors have collocated in at least 15 percent of the LEC's wire centers within an MSA, or have collocated in wire centers accounting for 30 percent of the LEC's revenues from these services within an MSA. Phase II pricing flexibility can be obtained if unaffiliated competitors have collocated in at least 50 percent of the LEC's wire centers within an MSA, or have collocated in wire centers accounting for 65 percent of the revenues from these services within an MSA. 47 C.F.R. §§ 69.709(b)-(c).

<sup>77</sup> See *Wireline Competition Bureau Seeks Comments on AT&T's Petition For Rulemaking to Reform Regulation of Incumbent Local Exchange Carrier Rates For Interstate Special Access Services*, RM No. 10593, DA 02-2913, (rel. Oct. 29, 2002), 17 FCC Rcd 21,530, 21,530.

<sup>78</sup> See, e.g., Letter from John E. Benedict, Sprint, Federal Regulatory Affairs-LDD, to Ms. Marlene H. Dortch, Secretary, Federal Communications Commission, CC Docket No. 01-338 (filed January 10, 2003); Nextel Reply Comments, CC Docket No. 01-338 at 7; and AT&T Wireless Comments, CC Docket No. 01-338 at 3.

<sup>79</sup> *Horizontal Merger Guidelines*, § 2.1.

<sup>80</sup> See, e.g., *Broadband NPRM*, 16 FCC Rcd at 22,762, para. 30; *In the Matter of Inquiry Concerning the Deployment of Advanced Telecommunications Capability to All Americans in a Reasonable and Timely Fashion, and Possible Steps to Accelerate Such Deployment Pursuant to Section 706 of the Telecommunications Act of 1996*, Report, 14 FCC Rcd 2398, 2423-24, para. 48 (1999).

<sup>81</sup> We note that similar price changes in a market do not necessarily indicate coordinated behavior, because changes in demand and supply conditions may equally affect all market participants.

anticompetitive price increase for interexchange service.<sup>82</sup> In addition, to what extent can mass market customers increase their use of mobile telephony services or Internet-based applications as a means of combating an anticompetitive price increase for in-region, interstate and international, interexchange telecommunications services whether imposed unilaterally by a carrier or by coordinated actions by a number of carriers?

34. Finally, the assessment of BOCs' and independent LECs' market power with respect to in-region, interstate and international interexchange telecommunications services market may differ across customer classes within a geographic market. We also seek comment on the relevance, if any, of the length of time since the BOC has received section 271 approval and whether it has received such approval in all of its in-region states. We request that commenters state whether their answers to the questions in this section are equally applicable to interstate and international interexchange services, and if not, to describe how they differ.

## **V. APPROPRIATE REGULATORY REQUIREMENTS**

### **A. Overview**

35. Once we have defined the relevant product and geographic markets for interexchange services, we can use this information to determine the appropriate classification of BOCs and independent LECs for the provision of in-region, interstate and international interexchange services. We can also determine what regulatory requirements, if any, are necessary to protect against potential harms to these markets that might result from BOCs' and independent LECs' market power in local exchange and exchange access markets. We ask interested parties to explain how their proposals address concerns regarding the ability of a BOC or an independent LEC to leverage its market power in the local exchange or exchange access markets to unlawful advantage in in-region, interstate and international interexchange markets. We request that interested parties discuss whether dominant carrier regulation of BOCs' and independent LECs' in-region, interstate and international interexchange services is necessary to prevent potential improper allocations of costs, discrimination against competitors, or price squeezes. In the alternative, we ask whether there may be less burdensome or more effective regulatory means available to guard against this potential behavior.

### **B. Classification of BOCs and Independent LECs for In-Region, Interstate and International Interexchange Services**

36. As discussed previously, the Commission has historically distinguished between dominant carriers, which possess individual market power, and non-dominant carriers, which lack individual market power.<sup>83</sup> Non-dominant carriers have been subject to significantly

<sup>82</sup> See, e.g., *Horizontal Merger Guidelines*, § 2.2. In some circumstances, coordinated interaction can be effectively prevented or limited by maverick firms – firms that have a greater economic incentive to deviate from the terms of coordination than do most of their rivals (e.g., firms that are unusually disruptive and competitive influences in the market). *Horizontal Merger Guidelines*, § 2.1.2.

<sup>83</sup> See Section II, *supra*.

reduced regulation. In contrast, dominant carriers are subject to a broad range of regulatory requirements that are generally intended to protect consumers from unjust and unreasonable rates, terms and conditions and unreasonable discrimination in the provision of communications services.<sup>84</sup>

37. Under the Commission's rules, non-dominant domestic carriers may file tariffs that are presumed lawful on one day's notice and without cost support, and they do not file tariffs at all for most interexchange services.<sup>85</sup> In contrast, dominant domestic carriers must file tariffs on 1 to 120 days' notice, with supporting information, including, in some cases, detailed cost data.<sup>86</sup> Moreover, the Commission's rules provide that an interstate interexchange carrier found to be dominant would be subject to price cap regulation, when specified by Commission order.<sup>87</sup> The Commission also requires any carrier classified as dominant for the provision of international services on a particular route for any reason other than a foreign carrier affiliation to file tariffs for those services, pursuant to the same notice and cost support requirements for tariff filings of dominant domestic carriers.<sup>88</sup>

### 1. BOC Classification

38. We ask whether, and to what extent, dominant carrier regulation of interstate and international interexchange services is suited to achieving the Commission's objectives to promote competition and to deter anticompetitive behavior by BOCs following a section 272 sunset. The regulatory requirements on a carrier classified as dominant in a particular market generally are designed to prevent a carrier from raising prices by restricting its output rather than to prevent a carrier from raising its prices by raising its rivals' costs; therefore, application of these regulations to a carrier that does not have the ability to leverage its market power by restricting its own output could lead to incongruous results.<sup>89</sup> The Commission has acknowledged that some dominant carrier regulations, such as formerly stringent section 214 requirements, were not designed to address the potential problems associated with BOC entry into competitive markets, and may not be the most efficient means of addressing the concerns raised by a BOC's entry into the long distance marketplace.<sup>90</sup> On the other hand, certain aspects

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<sup>84</sup> 47 U.S.C. §§ 201-202.

<sup>85</sup> See 47 C.F.R. §§ 61.19; 61.22-61.23; see also *LEC Classification Order*, 12 FCC Rcd at 15,766, para. 12 (citing *Tariff Filing Requirements for Non-Dominant Carriers*, CC Docket No. 93-36, Order, 10 FCC Rcd 13,653 (1995)). All interstate interexchange carriers are currently classified as non-dominant and are prohibited from filing tariffs except for the limited purposes contained in §§ 61.19(b) and (c) of the Commission's rules. See *Competitive Carrier First Report and Order*, 85 FCC 2d at 23, para. 63; *AT&T Reclassification Order*, 11 FCC Rcd at 3271.

<sup>86</sup> See 47 C.F.R. §§ 61.38, 61.58.

<sup>87</sup> See 47 C.F.R. §§ 61.3(ee), 61.41-61.49.

<sup>88</sup> See 47 C.F.R. § 61.28(a)-(b).

<sup>89</sup> See *LEC Classification Order*, 12 FCC Rcd at 15,804-05, paras. 85-86 (citations omitted).

<sup>90</sup> See *LEC Classification Order*, 12 FCC Rcd at 15,804-05, para. 86 (noting that "[b]ecause we have previously found that markets for long distance services are substantially competitive in most areas, marketplace forces should (continued....)

of dominant carrier regulation, including tariff filings with detailed cost support data and price cap regulations, may deter anticompetitive behavior such as predatory pricing.<sup>91</sup>

39. Commenters should address whether there are specific aspects of dominant carrier regulation that are necessary to constrain BOCs from engaging in certain types of anticompetitive behavior and whether specific aspects of the regulations do not address adequately potential problems that may arise in the interexchange marketplace, if there are no separate affiliate requirements. Commenters should also address the costs and benefits of regulation in this context and whether imposing dominant carrier regulation may, in fact, dampen competition, and whether there are other statutory and regulatory provisions in place or available that would accomplish the same objectives while imposing fewer burdens on the carriers and the Commission. For example, would requiring BOCs to file tariffs on advance notice and with cost support data impose more significant costs and burdens, or adversely affect competition, without offsetting benefits? Or, for example, do price cap regulations sufficiently reduce the risk of anticompetitive discrimination and improper allocation of costs in a less burdensome manner?

40. As a final matter, we request that interested parties address whether there are adequate safeguards in place, post-sunset, including existing forms of price cap regulation,<sup>92</sup> that would prevent anticompetitive conduct by BOCs, including cost misallocation, unlawful discrimination, or a price squeeze.<sup>93</sup> We invite interested parties to address whether existing provisions of the Act provide safeguards that may reduce the need for other forms of regulation. Moreover, we ask interested parties to address the development of competition in the provision of local exchange and exchange access services, and the existence of alternative technologies, such as fixed wireless, to provision these services and to provide alternative inputs to interexchange markets. We note that while we seek to minimize regulatory burdens on the BOCs, at the same time, we seek to avoid the potential exposure of both ratepayers in local markets and competitors in interexchange markets to the potential risk of improper cost allocation and unlawful discrimination. Accordingly, we ask parties to address whether any burdens that dominant carrier regulation may impose on BOCs outweigh any potential benefits.

## 2. Independent LEC Classification

41. In this proceeding, we also ask whether an independent LEC should be classified as dominant or non-dominant absent its adherence to the separate affiliate requirements, as set forth in the *LEC Classification Order*. While the Commission is already considering whether to eliminate the separate affiliate safeguards imposed on certain independent LECs when they

(Continued from previous page) \_\_\_\_\_  
effectively deter carriers that face competition from engaging in the practices that Congress sought to address through the section 214 requirements”).

<sup>91</sup> See *LEC Classification Order*, 12 FCC Rcd at 15,805-06, para. 87.

<sup>92</sup> We note that, pursuant to our *Pricing Flexibility Order*, certain BOCs and independent LECs have obtained pricing flexibility from price cap regulation for special access services in a number of markets. See *supra* para. 32; 47 C.F.R. § 69.727.

<sup>93</sup> *LEC Classification Order*, 12 FCC Rcd at 15,850, 15,852 paras. 163, 167.

provide in-region, interexchange services,<sup>94</sup> in this proceeding, we seek comment on the additional question of whether there is a need to regulate independent LECs as dominant should we remove the separate affiliate requirements and other safeguards established for facilities-based and reseller independent LECs.<sup>95</sup> We note that while the Commission previously determined that dominant carrier regulation of independent LECs' interstate and international interexchange services would be inappropriate,<sup>96</sup> it also concluded that retaining the *Fifth Report and Order* separation requirements for independent LECs would aid in prevention and detection of anticompetitive conduct, including cost misallocation, unlawful discrimination, or a price squeeze.<sup>97</sup>

42. As with the BOCs, we ask parties to consider whether, and to what extent, dominant carrier regulation is suited to achieving the Commission's objectives to promote competition and to deter anticompetitive behavior by independent LECs, should the Commission remove the *Fifth Report and Order* separation requirements. In particular, parties should address whether there are specific aspects of dominant carrier regulation that are necessary to constrain independent LECs from engaging in certain types of anticompetitive behavior if they provide interexchange service on a fully integrated basis. Parties should also consider whether specific aspects of the regulations do not address adequately potential problems that may arise in the interexchange marketplace, absent the separation requirements.

43. We also ask parties to consider each of the dominant carrier regulations currently in place and address whether, and to what extent, those regulations are necessary to address any risks associated with the independent LECs' provision of in-region, interstate and international interexchange services, absent the *Fifth Report and Order* requirements. We ask parties to take into account both the associated costs and benefits of dominant carrier regulation on independent LECs, and to consider whether potential predatory behavior is adequately addressed through other processes and requirements.<sup>98</sup> Finally, with respect to independent LECs as resellers, we seek comments regarding whether any dominant or non-dominant regulatory classification and rules adopted in this proceeding with respect to facilities-based independent LECs should apply

<sup>94</sup> See 2000 Biennial Regulatory Review, 16 FCC Rcd at 17,270.

<sup>95</sup> As noted earlier, in the *Second Reconsideration Order*, the Commission reaffirmed its basic analytical framework, while relaxing its requirements to permit the use of a separate corporate division by independent LECs that provide in-region, interexchange services exclusively through resale. *Second Reconsideration Order*, 14 FCC Rcd at 10,771, 10,790-91, para. 26.

<sup>96</sup> *LEC Classification Order*, 12 FCC Rcd at 15,848, para. 158 (concluding that the Commission should not apply dominant carrier regulation to independent LECs as such regulation was "not necessary to prevent, nor effective in detecting improper cost allocation, unlawful discrimination, price squeezes, or other anticompetitive conduct").

<sup>97</sup> *LEC Classification Order*, 12 FCC Rcd at 15,850, 15,852 paras. 163, 167.

<sup>98</sup> See, e.g., *LEC Classification Order*, 12 FCC Rcd at 15,854-55, para. 171 (stating that the benefits of dominant carrier regulation are outweighed by the burdens imposed on independent LECs and noting that the Commission's complaint process, enforcement of antitrust laws and access charge reform address or mitigate some predatory behavior).

equally to those independent LECs that provide in-region, interexchange services exclusively through resale. If a different outcome is appropriate, including maintaining the current safeguards for independent LEC resellers, we ask parties to explain why.

### 3. In-Region, International Interexchange Services

44. As the Commission has previously determined, there appear to be no practical distinctions between a BOC's or an independent LEC's ability to engage in anticompetitive behavior against unaffiliated domestic interexchange competitors as opposed to international competitors.<sup>99</sup> We ask interested parties to address whether any regulatory classification and accompanying requirements we adopt in this proceeding for a BOC's or independent LEC's provision of in-region, interstate interexchange services should apply equally to its provision of in-region, international interexchange services. Parties should address whether there are considerations particular to the provision of international services that warrant differing treatment or unique concerns that warrant particularized rules.

#### C. Alternative Regulatory Approaches

45. As described above, even if the section 272 separate affiliate and related requirements sunset, the statute specifies that the requirements of section 272(e) do not sunset. The Commission has interpreted this to mean that the requirements of sections 272(e)(1) and (3) remain post-sunset.<sup>100</sup> These safeguards require BOCs: (1) to fulfill requests from unaffiliated entities for telephone exchange service and exchange access within a period no longer than the period in which the BOC provides such telephone exchange service and exchange access to itself; and (2) to impute to themselves, an amount for telephone exchange service and exchange access, not less than that charged to unaffiliated interexchange carriers.<sup>101</sup> Further, the Commission's existing authority is preserved under section 272(f)(3), which provides that the Commission's authority under any other section of the Act to prescribe safeguards consistent with the public interest shall not be limited by the sunset provisions.<sup>102</sup>

46. We ask interested parties to comment on whether, and in what manner, the statutory requirements that continue to apply to BOCs under section 272(e) reduce the need for dominant carrier regulations. We ask parties to address whether sections 272(e)(1) and (3) provide adequate safeguards to deter anticompetitive behavior, and whether the Commission

<sup>99</sup> *LEC Classification Order*, 12 FCC Rcd at 15,838, 15,862-63 paras. 138, 188. As explained previously, we do not intend, in this docket, to address the classification of BOCs or independent LECs as "dominant" on specific routes in their provision of international services under 47 C.F.R. § 63.10 of the Commission's rules, which addresses foreign carrier affiliations. See note 1 *supra*.

<sup>100</sup> The Commission has previously determined that the non-discrimination obligations imposed by subsections 272(e)(2) and 272(e)(4) are framed in reference to a BOC's treatment of its affiliates and thus, are only applicable if a BOC maintains a separate affiliate. *Non-Accounting Safeguards Order*, 11 FCC Rcd at 22,035, para. 270.

<sup>101</sup> 47 C.F.R. §§ 272(e)(1) & (3).

<sup>102</sup> 47 C.F.R. § 272(f)(3).

should rely on enforcement activity alone or should adopt additional prophylactic requirements to implement these provisions. For example, with respect to prophylactic requirements, would the separate affiliate requirements that are currently applicable to independent LECs be appropriate to apply to the BOCs?<sup>103</sup> We also ask parties to comment on the Commission's interpretation of sections 272(e)(2) and (4) as inapplicable if a BOC no longer retains a separate affiliate, and whether the Commission should consider an alternative interpretation of sections 272(e)(2) and (4) that would support the application of these sections post-sunset.

47. Section 272(e)(1) requires that a BOC fulfill requests from unaffiliated entities at least as quickly as it fulfills its own.<sup>104</sup> The Commission has previously concluded that, to implement this statutory directive, the response time in which a BOC provides such requests should be no greater than the response time it provides to itself, and that the BOC must make information regarding the service intervals it provides to itself available to unaffiliated entities.<sup>105</sup>

We seek comment on the ability and opportunity for BOCs to discriminate in the fulfillment of requests from unaffiliated interexchange carriers. We note that industry standards and processes for access services provided by BOCs to interexchange carriers are significantly more developed than those used for network elements ordered from BOCs by competitive LECs. Do these standards and processes reduce or eliminate the ability of a BOC to engage in unlawful activity? We also note that the Commission has released two Notices addressing national performance measurements and standards, in the Unbundled Network Element and Special Access Measurements and Standards proceedings.<sup>106</sup> We ask that parties comment on whether adoption of the measures considered in these proceedings would provide sufficient post-sunset safeguards. Moreover, would Commission action implementing measurements and standards for special access services appropriately implement section 272(e)(1) or are there other ways to implement this provision? We seek comment on whether similar measures would be appropriate to apply to independent LECs.

48. We ask interested parties to consider the requirements of section 272(e)(3) regarding a BOC's pricing to unaffiliated providers. In particular, is the requirement that the BOC impute to itself an amount for access that is no less than the amount charged to any unaffiliated interexchange carrier for such service sufficient to detect and deter pricing discrimination or a price squeeze? We seek comment on the specific ability and opportunity for BOCs to discriminate in their pricing to unaffiliated providers. We ask parties to discuss whether additional safeguards are necessary to prevent cost misallocation and to more fully implement the imputation requirement of the statute. Parties should also consider whether existing Commission

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<sup>103</sup> See generally *Competitive Carrier Fifth Report and Order*, 98 FCC 2d at 1191.

<sup>104</sup> 47 C.F.R. § 272(e)(1).

<sup>105</sup> *Non-Accounting Safeguards Order*, 11 FCC Rcd at 22,019-20, paras. 240-242.

<sup>106</sup> *Performance Measurements and Standards for Unbundled Network Elements and Interconnection*, et al., CC Docket No. 01-318, Notice of Proposed Rulemaking, 16 FCC Rcd 21,428 (2001); *Performance Measurements and Standards for Interstate Special Access Services*, et al., CC Docket No. 01-321, Notice of Proposed Rulemaking, 16 FCC Rcd 22,117 (2001).



rules would be sufficient safeguards if applied to a BOC's provision of in-region, interstate and international interexchange telecommunications services. For example, would the Commission's cost allocation rules, which are intended to prevent cross-subsidization and cost misallocation for regulated and nonregulated activities and competitive and noncompetitive services, serve as an effective alternative to a separate affiliate requirement?<sup>107</sup> In looking at this approach, we ask parties to consider the advantages and disadvantages of treating BOC in-region, interstate and international interexchange services as a regulated activity under Part 64 of our rules. We ask parties to discuss whether this approach is burdensome relative to the potential benefits, and whether modification of these requirements would be necessary to address continued discrimination concerns. We seek comment on whether similar measures would be appropriate to apply to independent LECs.

49. We also seek comment on how the Commission should treat the independent LECs' provision of long distance on an integrated basis and whether it would be appropriate to apply any of the alternative regulatory approaches discussed in this section to independent LECs. To the extent commenters believe that different safeguards should apply to BOCs and independent incumbent LECs, they should explain their reasoning.

## VI. PROCEDURAL MATTERS

### A. *Ex Parte* Presentations

50. These matters shall be treated as a "permit-but-disclose" proceeding in accordance with the Commission's *ex parte* rules.<sup>108</sup> Persons making oral *ex parte* presentations are reminded that memoranda summarizing the presentations must contain summaries of the substance of the presentations and not merely a listing of the subjects discussed. More than a one or two sentence description of the views and arguments presented is generally required.<sup>109</sup> Other requirements pertaining to oral and written presentations are set forth in section 1.1206(b) of the Commission's rules.

### B. Initial Paperwork Reduction Act Analysis

51. This *Further NPRM* may modify an information collection. As part of our continuing effort to reduce paperwork burdens, we invite the general public and the Office of Management and Budget (OMB) to take this opportunity to comment on the possible changes in information collection contained in the *Further NPRM*, as required by the Paperwork Reduction Act of 1995, Pub. L. No. 104-13. Public and agency comments are due 60 days from the date of publication of this *Further NPRM* in the Federal Register. Comments should address: (1) whether the possible changes in the collections of information are necessary for the proper performance of the functions of the Commission, including whether the information will have

<sup>107</sup> See 47 C.F.R. §§ 64.901-64.905.

<sup>108</sup> 47 C.F.R. §§ 1.1200-1.1216.

<sup>109</sup> See 47 C.F.R. § 1.1206(b)(2).

practical utility; (2) the accuracy of the Commission's burden estimates; (3) ways to enhance the quality, utility, and clarity of any information collected; and (4) ways to minimize the burden of any collection of information on the respondents, including the use of automated collection techniques or other forms of information technology.

### C. Comment Filing Procedures

52. Pursuant to sections 1.415 and 1.419 of the Commission's rules,<sup>110</sup> interested parties may file comments within 30 days after publication of this Further Notice in the Federal Register and may file reply comments within 60 days after publication of this Further Notice in the Federal Register. All filings should refer to WC Docket No. 02-112 and CC Docket No. 00-175. Comments may be filed using the Commission's Electronic Comment Filing System (ECFS) or by filing paper copies.<sup>111</sup> Comments filed through ECFS can be sent as an electronic file via the Internet to <http://www.fcc.gov/e-file/ecfs.html>. Generally, only one copy of an electronic submission must be filed. In completing the transmittal screen, commenters should include their full name, postal service mailing address, and the applicable docket number(s), which in this instance are WC Docket No. 02-112 and CC Docket No. 00-175. Parties may also submit an electronic comment by Internet e-mail. To get filing instructions for e-mail comments, commenters should send an e-mail to [ecfs@fcc.gov](mailto:ecfs@fcc.gov), and should include the following words in the subject line of the message: "get form <your e-mail address>." A sample form and directions will be sent in reply.

53. Parties who choose to file by paper should also submit their comments on diskette. These diskettes should be submitted to Janice Myles, Competition Policy Division, Wireline Competition Bureau, Federal Communications Commission, 445 12<sup>th</sup> Street S.W., Washington, D.C. 20554. Such a submission should be on a 3.5 inch diskette formatted in an IBM compatible format using Microsoft Word or compatible software. The diskette should be accompanied by a cover letter and should be submitted in "read only" mode. The diskette should be clearly labeled with the commenter's name, proceeding (including the docket number(s), in this case, WC Docket No. 02-112 and CC Docket No. 00-175), type of pleading (comment or reply comment), date of submission, and the name of the electronic file on the diskette. The label should also include the following phrase: "Disk Copy -- Not an Original." Each diskette should contain only one party's pleading, preferably in a single electronic file. In addition, commenters must send diskette copies to the Commission's copy contractor, Qualex International, Portals II, 445 12<sup>th</sup> Street S.W., CY-B402, Washington, D.C. 20554.

54. Regardless of whether parties choose to file electronically or by paper, parties should also file one copy of any documents filed in this docket with the Commission's copy contractor, Qualex International, Portals II, 445 12<sup>th</sup> Street S.W., CY-B402, Washington, D.C. 20554 (telephone 202-863-2893; facsimile 202-863-2898) or via e-mail at [qualexint@aol.com](mailto:qualexint@aol.com).

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<sup>110</sup> 47 C.F.R. §§ 1.415, 1.419.

<sup>111</sup> See *Electronic Filing of Documents in Rulemaking Proceedings*, 63 Fed. Reg. 24,121 (1998).

55. Comments and reply comments must include a short and concise summary of the substantive arguments raised in the pleading. Comments and reply comments must also comply with section 1.48 and all other applicable sections of the Commission's rules.<sup>112</sup> We direct all interested parties to include the name of the filing party and the date of the filing on each page of their comments and reply comments. All parties are encouraged to utilize a table of contents, regardless of the length of their submission. We also strongly encourage that parties track the organization set forth in the Further Notice in order to facilitate our internal review process.

#### **D. Initial Regulatory Flexibility Analysis**

56. As required by the Regulatory Flexibility Act of 1980, as amended (RFA),<sup>113</sup> the Commission has prepared the present Initial Regulatory Flexibility Analysis (IRFA) of the possible significant economic impact on a substantial number of small entities by the policies and rules proposed in this Further Notice.<sup>114</sup> Written public comments are requested on this IRFA. Comments must be identified as responses to the IRFA and must be filed by the deadlines for comments on the Further Notice provided above. The Commission will send a copy of the Further Notice, including this IRFA, to the Chief Counsel for Advocacy of the Small Business Administration.<sup>115</sup> In addition, the Further Notice and IRFA (or summaries thereof) will be published in the Federal Register.<sup>116</sup>

#### **1. Need for, and Objectives of, the Proposed Rules**

57. In this proceeding, we seek comment on: (1) the appropriate regulatory classification of BOCs for the provision of in-region, interstate and international interexchange services post sunset of the section 272 safeguards; (2) the appropriate regulatory classification of independent LECs for the provision of in-region, interstate and international interexchange services absent the *Fifth Report and Order* requirements; (3) the relevant identification of service markets affecting the provision of in-region, interstate and international interexchange services; and (4) the appropriate regulatory requirements for the provision of in-region, interstate and international interexchange services by BOCs and independent LECs, given current market conditions. The basic elements of the existing dominant carrier regulatory requirements were initially developed some twenty-five years ago and have focused on constraining the ability of dominant carriers to exercise market power. Application of these requirements to carriers without the ability to leverage market power by restricting output could lead to incongruous results. Thus, we ask interested parties to address whether dominant carrier regulations are well

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<sup>112</sup> See 47 C.F.R. § 1.48.

<sup>113</sup> See 5 U.S.C. § 603. The RFA, see 5 U.S.C. §§ 601-612, has been amended by the Small Business Regulatory Enforcement Fairness Act of 1996 (SBREFA), Pub. L. No. 104-121, 110 Stat. 857 (1996).

<sup>114</sup> We also expect that we could certify this FNPRM under 5 U.S.C. § 605, because, as we describe in this IFRA, our proposed actions, if adopted, would lessen compliance burdens on affected entities.

<sup>115</sup> See 5 U.S.C. § 603(a).

<sup>116</sup> See *id.*

or ill-suited to prevent the risks associated with the BOCs' and independent LECs' provision of in-region, interstate and international interexchange services post section 272 sunset (for the BOCs) and absent the separation safeguards (applicable to independent LECs). We also request that parties address how the Commission can best balance the goals of deterring BOC and independent LEC anticompetitive and discriminatory behavior and eliminating unnecessary regulation.

## 2. Legal Basis

58. The legal basis for any action that may be taken pursuant to the Further Notice is contained in sections 1, 2, 4(i)-4(j), 201, 202, 272 and 303(r) of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151, 152, 154(i)-4(j), 201, 202, 272 and 303(r).

## 3. Description and Estimate of the Number of Small Entities to Which the Proposed Rules will Apply

59. The RFA directs agencies to provide a description of and, where feasible, an estimate of the number of small entities that will be affected by the proposed rules.<sup>117</sup> The RFA generally defines the term "small entity" as having the same meaning as the terms "small business," "small organization," and "small governmental jurisdiction."<sup>118</sup> In addition, the term "small business" has the same meaning as the term "small business concern" under the Small Business Act.<sup>119</sup> A small business concern is one which: (1) is independently owned and operated; (2) is not dominant in its field of operation; and (3) satisfies any additional criteria established by the Small Business Administration (SBA).<sup>120</sup>

60. We have included small incumbent LECs in this present RFA analysis. As noted above, a "small business" under the RFA is one that, *inter alia*, meets the pertinent small business size standard (e.g., a telephone communications business having 1,500 or fewer employees), and "is not dominant in its field of operation."<sup>121</sup> The SBA's Office of Advocacy contends that, for RFA purposes, small incumbent LECs are not dominant in their field of operation because any such dominance is not "national" in scope.<sup>122</sup> We have therefore included

<sup>117</sup> 5 U.S.C. §§ 603(b)(3), 604(a)(3).

<sup>118</sup> *Id.* § 601(6).

<sup>119</sup> 5 U.S.C. § 601(3) (incorporating by reference the definition of "small business concern" in the Small Business Act, 15 U.S.C. § 632). Pursuant to 5 U.S.C. § 601(3), the statutory definition of a small business applies "unless an agency, after consultation with the Office of Advocacy of the Small Business Administration and after opportunity for public comment, establishes one or more definitions of such terms which are appropriate to the activities of the agency and publishes such definition(s) in the Federal Register."

<sup>120</sup> *Id.* § 632.

<sup>121</sup> *Id.*

<sup>122</sup> Letter from Jere W. Glover, Chief Counsel for Advocacy, SBA, to William E. Kennard, Chairman, FCC (May 27, 1999). The Small Business Act contains a definition of "small business concern," which the RFA incorporates (continued....)

small incumbent LECs in this RFA analysis, although we emphasize that this RFA action has no effect on FCC analyses and determinations in other, non-RFA contexts.

61. *Incumbent Local Exchange Carriers.* Neither the Commission nor the SBA has developed a small business size standard specifically directed toward providers of incumbent local exchange service. The closest applicable size standard under the SBA rules is for Wired Telecommunications Carriers.<sup>123</sup> This provides that such a carrier is small entity if it employs no more than 1,500 employees.<sup>124</sup> Commission data from 2000 indicate that there are 1,329 incumbent local exchange carriers, total, with approximately 1,024 having 1,500 or fewer employees.<sup>125</sup> The small carrier number is an estimate and might include some carriers that are not independently owned and operated; we are therefore unable at this time to estimate with greater precision the number of these carriers that would qualify as small businesses under SBA's size standard. Consequently, we estimate that there are no more than 1,024 ILECS that are small businesses possibly affected by our action.

#### 4. Description of Projected Reporting, Recordkeeping and Other Compliance Requirements

62. We expect that any proposal we may adopt pursuant to this Further Notice will decrease existing reporting, recordkeeping or other compliance requirements. As noted above, dominant carriers are currently subject to a broad range of regulatory requirements that are generally intended to protect consumers from unjust and unreasonable rates, terms, and conditions and unreasonable discrimination in the provision of communications services.<sup>126</sup> The Commission's dominant carrier regulation includes rate regulation and tariff filing requirements,<sup>127</sup> and also requires supporting information, which in some cases includes detailed cost data, to be filed by dominant carriers with their tariff filings.<sup>128</sup> Moreover, the Commission

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into its own definition of "small business." See 15 U.S.C. § 632(a) (Small Business Act); 5 U.S.C. § 601(3) (RFA). SBA regulations interpret "small business concern" to include the concept of dominance on a national basis. 13 C.F.R. § 121.102(b).

<sup>123</sup> 13 C.F.R. § 121.201, NAICS Code 517110.

<sup>124</sup> *Id.*

<sup>125</sup> FCC, Wireline Competition Bureau, Industry Analysis and Technology Division, "Trends in Telephone Service" at Table 5.3, page 5-5 (May 2002).

<sup>126</sup> See Section II, *supra*.

<sup>127</sup> Section 203(a) of the Communications Act generally requires common carriers to file tariffs governing the provision of their basic communications services, although section 203(b)(2) gives the Commission broad authority to modify requirements made pursuant to this authority. 47 U.S.C. §§ 203(a) & (b)(2) (1996).

<sup>128</sup> 47 C.F.R. §§ 61.38-39, 61.58 (1999). Non-dominant IXC's are prohibited from filing tariffs except for the limited purposes contained in 61.19(b) and (c). Non-dominant (competitive) LECs are permitted to tariff access charges within the limits set in the *CLEC Access Charge Order*, but may not tariff charges above those benchmarks. *CLEC Access Charge Order*, 16 FCC Rcd at 9925, para. 3.

has international dominant carrier tariff filing requirements.<sup>129</sup> This Further Notice seeks comment on whether continued dominant carrier regulation is appropriate post sunset of the section 272 separate affiliate requirements on a state-by-state basis, and whether it is necessary to streamline or modify the traditional dominant carrier regulations of BOCs' provision of in-region, interstate and international interexchange services. This Further Notice also seeks comment on whether dominant carrier regulation of independent LECs is necessary should the Commission eliminate the separation requirements currently imposed on such carriers for their provision of in-region, interstate and international interexchange services.

#### **5. Steps Taken to Minimize Significant Economic Impact on Small Entities, and Significant Alternatives Considered**

63. The RFA requires an agency to describe any significant, specifically small business, alternatives that it has considered in reaching its proposed approach, which may include the following four alternatives (among others): (1) the establishment of differing compliance or reporting requirements or timetables that take into account the resources available to small entities; (2) the clarification, consolidation, or simplification of compliance or reporting requirements under the rule for small entities; (3) the use of performance, rather than design, standards; and (4) an exemption from coverage of the rule, or any part thereof, for small entities.<sup>130</sup>

64. The overall objective of this proceeding is to reduce regulatory burdens on BOCs and independent LECs to the extent consistent with the public interest. The Further Notice seeks specific proposals as to which existing regulations might be removed or streamlined in their application to a BOCs' or independent LECs' provision of interstate and international interexchange services absent current safeguards, and asks parties to comment on whether BOCs and independent LECs should be classified as non-dominant in the provision of such services post sunset or, in the case of independent LECs, once separation safeguards are removed.<sup>131</sup> The Further Notice also asks parties to discuss whether, and to what extent, dominant carrier regulation is aptly suited to achieving the Commission's objectives to promote competition and to deter anticompetitive behavior by BOCs and independent LECs. This Further Notice addresses whether there are specific aspects of dominant carrier regulation that continue to be necessary to constrain BOCs and independent LECs from engaging in certain types of anticompetitive behavior, and whether there are specific aspects of the regulations that do not address potential problems that may arise in the interexchange marketplace, absent the separate affiliate requirements. Again, we seek comment on these matters, especially as they might affect small entities subject to the rules.

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<sup>129</sup> See 47 C.F.R. § 61.28(a).

<sup>130</sup> 5 U.S.C. § 603(c).

<sup>131</sup> See Section I, *supra*.

**6. Federal Rules that May Duplicate, Overlap, or Conflict with the Proposed Rules**

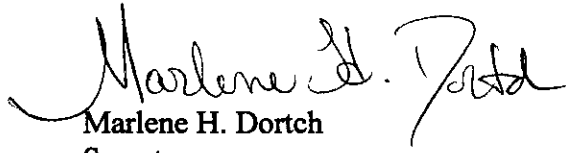
65. None.

**VII. ORDERING CLAUSES**

66. Accordingly, IT IS ORDERED that, pursuant to the authority contained in sections 1, 2, 4(i)-4(j), 201, 202, 272 and 303(r) of the Communications Act of 1934, as amended, 47 U.S.C. §§ 151, 152, 154(i)-4(j), 201, 202, 272 and 303(r), this Further Notice IS ADOPTED.

67. IT IS FURTHER ORDERED that the Commission's Consumer and Governmental Affairs Bureau, Reference Information Center, SHALL SEND a copy of this Further Notice, including the Initial Regulatory Flexibility Analysis, to the Chief Counsel for Advocacy of the Small Business Administration.

FEDERAL COMMUNICATIONS COMMISSION

  
Marlene H. Dortch  
Secretary

**JOINT STATEMENT OF  
COMMISSIONER MICHAEL J. COPPS AND  
COMMISSIONER JONATHAN S. ADELSTEIN,  
CONCURRING**

Re: *Section 272(f)(1) Sunset of the BOC Separate Affiliate and Related Requirements (WC Docket No. 02-112); 2000 Biennial Regulatory Review Separate Affiliate Requirements of Section 64.1903 of the Commission's Rules (CC Docket No. 00-175)*

Today the Commission seeks comment on how changes to the competitive landscape impact the provision of in-region long distance service. We choose to concur because we have some concerns with the approach the Commission has taken in the past on similar issues and because we are concerned that this particular item's construction could bias the outcome of our current proceeding.

Last December, the Commission decided to allow the separate affiliate requirements in section 272 to sunset in New York. This was done without, we believed, the detailed requisite market analysis and over the objections of our state colleagues.

By revisiting these issues now in this proceeding, the Commission has an opportunity to get them right. Structural and accounting safeguards are our principal guarantees against improper accounting practices and cross-subsidizations. In an era of corporate governance problems and accounting depredations, this Commission has an especially high burden to overcome if it chooses to eliminate or reduce the separate affiliate protections that help prevent and detect anticompetitive behavior. The record generated in response to today's item is critical. To conduct an analysis with appropriate rigor, we ask commenters to address not only competition in the end-user market for long distance service, but the access market where the Commission previously has acknowledged that incumbents have the incentive and ability to exercise market power through control of local bottleneck facilities. We also encourage commenters to address what, if anything, has changed since the Commission last spoke to these issues in the *LEC Classification Order*. With the state of competition in our long distance markets at stake, we warn that cursory analysis based on weak economics will not suffice.

We are pleased that the Commission will review these issues for both Bell Operating Companies and rural independent carriers in a coherent and reasoned single proceeding. Like our colleagues, we intend to review the record closely, study the merits of all possible outcomes and determine what safeguards, if any, are necessary to prevent anticompetitive discrimination in the market.

Our concern is that this item might be interpreted by some as leading toward a predetermined outcome. What we are in search of here is absence of such an outcome and the reality of an open and unbiased record. We look forward to doing everything we can, with the Bureau and our colleagues, to make that happen.